



INNOVATIONS FOR SUCCESSFUL SOCIETIES

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Interviewee: Mahmoud Mohieldin

Interviewer: Deepa Iyer

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Innovations for Successful Societies, Bobst Center for Peace and Justice
Princeton University, 83 Prospect Avenue, Princeton, New Jersey, 08544, USA
www.princeton.edu/successfulsocieties

IYER: The administrative reforms behind the economic reforms in Egypt really interest us. One question that I had was: Back in 2004, when the Ahmed Nazif government came in, what were the key motivations for this reform? What were the driving forces behind the reforms?

MOHIELDIN: *Well, I think it's basically the conditions of the economy and the financial sector at the time that pushed the government of Egypt in July 2004 to get itself into a sort of a comprehensive reform program. Matters were not really looking good by using the conventional indicators. And it's not just the financial sector—it's the overall economic and development performance. Measuring Egypt to itself or measuring Egypt to its neighborhood was basically showing that a lot is needed for the reforms.*

Growth was very low, ranging between 3 percent and 3.5 percent, real terms. This was basically a case of recession or stagnation for a developing country, especially a developing country facing problems of dealing with poverty, high unemployment rates, low incomes. So, we do not really have the luxury of growing at this low rate, especially when the population growth is—and still is—high, as in the case of Egypt. So, we need to do efforts for catch-up growth and for getting into the development policies fast.

IYER: What were the main challenges facing the banking sector and the central bank internally at this time?

MOHIELDIN: *Well, basically the usual problems of developing countries. Though Egypt didn't really have what could be classified as a crisis of such, there was a variety of problems: under-capitalization; low performance as measured by return on income or equity or assets of the banks; very low competition levels. The system was not really able to meet the growing demands for credit. The system was very much over-banked and under-branched. But primarily the case of the NPLs (non-performing loans) was very worrisome. This was well before the international financial crisis—but immediately after the emerging-markets crisis. So, there were lessons as well drawn from the emerging-markets crisis of the Asian countries of the 1990s.*

IYER: I understand that a central banking law was passed in 2003, which really set the stage for insuring the independence and regulatory authorities of the central bank. A new board of directors and a new governor were appointed later, in December of 2003. I was wondering if you have any information about this law, who was behind it, and why it occurred at this time specifically?

MOHIELDIN: *Well, I was very much behind it myself, among others. I worked for a while as a senior adviser to the minister of economy and trade. I was the chairman of the economic committee of the National Democratic Party, and I was a member of the Central Bank of Egypt at that time.*

So, it first started with the issue of independence, from a note that was produced by the Ministry of Economy. And it was very much a unique case that government is pushing for the independence of the central bank and all aspects of its activities in the monetary-policy front and in bank supervision. I adopted that further through my work in the National Democratic Party. You will refer to the Egyptian newspapers, and this was basically before the time of the new management of the central bank, which was basically a blessing because you

can always have laws, but it's basically the powers of implementation and coordination that makes laws' relevance.

So, we drafted that law in the National Democratic Party, and I was very much pleased to say that it got good support by Parliament and government. And at the same time, it was one of the laws that didn't receive major changes and the drafting of articles, because it was very carefully designed. And it put the pillars and the anchors for applying independence—all of the elements of independence of the central bank are reflected in that law. All of the elements of corporate governance, information disclosure and transparency were reflected there, giving the central bank, as well, the authority for conducting monetary policy and applying the prudential-regulation rules.

We put a mechanism as well that sometimes has worked, sometimes hasn't, depending on priorities. That is basically the issue of coordination through an institutionalization of coordination. I can always meet with you occasionally, informally, and coordinate if you are the central bank and I am the government. But to have regular meetings and to agree on targets—but leaving the central bank to conduct the monetary policy to achieve the targets of monetary policies—was basically one of the main things that had been there in the law.

Some of the provisions in the law were made to be open-ended, because we understood at that time that there are many changes in the prudential-regulation measure that should be within the power of the central bank to get them done.

IYER: Specifically, this law was very much an effort that was spearheaded by the NDP's (National Democratic Party's) economic committee. Is that correct?

MOHIELDIN: *There was some sort of understanding of its importance by government, and the laws existing at the time were basically made in 1950s, they were made in 1970s, and some few amendments in the early 1990s. So a new comprehensive central-banking and foreign-exchange management code was very much needed.*

IYER: You mentioned that this was very much needed, and I was wondering if you could speak more at length about the internal challenges that the central bank was facing at that time.

MOHIELDIN: *I think the issue of implementation was very much understood by the new management of the central bank, which is the current management of the central bank. They know very well it's not just by laws and powers and independence that the world is going to be moving ahead, but they needed to empower the central bank—training, staffing, new recruits in all departments. And it was done in a very good way, by keeping and enhancing the skills and the capacity of the members of the central bank, and bringing a new caliber, and having a good approach in getting all of the teams to work together in harmony.*

And this was a very hard thing to do, especially in that you are required to do that while the economy is running, the monetary challenges are there, the banking challenges are there. So we don't really have the luxury of those who would close their shop for a few days or weeks to appear a better shape to their clients. You need to do that while you maintain the monetary developments and the banking requirements.

So I would really recognize with appreciation the leadership of the governor of the central bank, Dr. Farouk El Okdah, and his team. And I had the pleasure of working with that team formally as a member of the board for a few months, before my appointment as a minister, and then I continued the work and coordination.

IYER: Going back to the Central Banking Law, I understand that there is a later amendment to this law, specifically that Dr. El Okdah had to amend the law to revise remuneration schedules in order to recruit talent.

MOHIELDIN: *Yes, this was done in 2005, yes.*

IYER: Could you elaborate on this amendment?

MOHIELDIN: *Well, it was just an amendment in the law, and you can see it actually on the Web site of the central bank and in the documents of Parliament, because every new law, every amendment basically had to be fully justified. And the law itself gave those kinds of flexibility for adequate remuneration and support to the members on the central bank and the banking sector at large, and giving the capacity of the bank management to have some allocations and particular funds for enhancing the capacity of the workers.*

There have been some other changes as well, in the rules on monitoring banks and their clients, but there are not many. I think they took only one session in Parliament and they were very much straightforward. But the main pillars and the new framework were very much established in the law itself.

IYER: The central-banking law was passed, I believe, in June 2003, and then the new board of directors was hired in December. How were these individuals brought on board? Who was responsible for this change, since it occurred before the Ahmed Nazif government came to power in 2004.

MOHIELDIN: *By law, the board is appointed by the president. And this went through the usual procedures of selection of heads of institutions. Some of the members were known; the governor of the central bank was already the head of the biggest commercial bank in Egypt. Some of the members were already members of the old board. Some new faces were added. And then matters had their own dynamics for the successive boards.*

IYER: As an observer and a participant in these reforms, and a member of the board of directors at the central bank, what would you pinpoint as the key changes in the central bank since 2004?

MOHIELDIN: *The key changes—I just highlighted one of them as basically the new management, with the capacity of leading and the power and efficiency to get things done. Meanwhile, there had been some good coordination. The central bank and the country at large were basically blessed by very good conditions as far as the global economy and the emerging markets are concerned. Here, we are talking about 2003 until 2008.*

But starting in 2008, and it could be a few months before that, there had been some major challenges in terms of the food crisis, the volatility in fuel prices, and then the financial crisis, in addition to some incidents that affected the tourism sector. And these were all good tests for the bank and its capacity to deal with the problems and to adopt effective, preventive and accommodative measures.

And now with the measurement of success of the central bank despite all the constraints, the central bank managed to do well—in terms of banking reforms, management of capital flows, accumulation of international reserves, stability in the foreign-exchange market, and bringing trust and confidence in the central bank.

IYER: One thing that we're very interested in is the civil-service reform effort, you could say, within the central bank—in terms of how pay incentives were linked to performance. This is something I know that was done in the Ministry of Investment, as well.

MOHIELDIN: *Yes, fortunately, the central bank had more flexibility than the usual government departments, by having this kind of legal status that allowed the central bank to deal with the issues related to remuneration and having adequate support for the staff. And in areas like central banking, you cannot just assume that, by good measures and good laws, life is going to be nice and easy.*

So, this was not part of the civil-service reform that is very complicated, that takes time, and all of that. The Ministry of Investment along with the Ministry of Finance adopted their own policies. The Ministry of Investment was newly created, so we had a smaller number of staff within the ministry itself. Although this small number of staff was responsible for overseeing around 350,000 persons working in holding companies, affiliate companies, authorities, I kept the ministry very small and efficient.

I remember that when I was a senior adviser to the minister of economy, I went to visit one of the ministries in the Netherlands, and I asked them about the number of staff. And it was basically one-tenth the number of staff of our ministry, which was recognized as a small one in Egypt, the Ministry of Economy. And that ministry had more responsibilities than our Ministry of Economy and Trade.

So, I got their own charter of work and bylaws, and I remember briefing the minister then. I told him one of the dreams is basically to have this kind of light structure and effective way of management, to be away from all of these bureaucratic hassles, and to have this kind of approach like an octopus. I'm thinking here of the positive part of it—to have this kind of small head, but with a good grip and grasping of functions and activities in the affiliated entities. That was very good—for coordination; no waste of money or time; efficiency; effectiveness; doing well within very limited budget. And we got things done. But I had the luxury of that.

The Ministry of Finance had to create a sort of parallel system, like the Office of the Minister and other entities. This is another way, but while you are improving the old traditional and conventional system, it takes awhile. You need really to attend to managing critical issues, and again, you don't really have the luxury of "Let's wait until matters are going to be fixed." So, this kind of a parallel system has to be designed carefully, with an approach of convergence, that the new should meet the old and coordinate effectively with it.

IYER: Yes, definitely.

MOHIELDIN: *I have to say [interruption].*

IYER: Unlike the Ministry of Investment, the central bank was not starting with mostly new staff. There was a large recruitment drive, but at the same time there were quite a few inherited employees. Could you reflect on this and whether this was a major challenge that the bank faced at that time?

MOHIELDIN: *That's always a challenge. It's like—coming from Egypt with its 5,000 years of civilization—to have a new building built, modern, fully conditioned, environmentally friendly, and all of that, is an easier task than your work on conservation, for instance, or trying to fix an old building and make it relevant to the new world. Something of that nature happens with people as well. People were trained—some of them in a very good way, but it could be relevant to subjects that are not relevant any more.*

The central bank had been investing well in its people through training. So there was basically a need for this kind of good maneuvering, a good pilot, and a good leader—to get the best out of the people and, at the same time, to bring some new talents and skills, and integrate them all together. I bet that today, if you go to the central bank, you wouldn't really recognize who's new and who's old, because all the people are going and marching in the same direction.

IYER: Within the broader financial-sector reform effort, there must have been quite a bit of in-built resistance. Could you reflect on specifically what the main sources of resistance encountered were?

MOHIELDIN: *In where?*

IYER: Within the broader financial-sector reform, where did the main sources of resistance come from?

MOHIELDIN: *Well, people normally would say, "Transfer of ownership from public to private sector is a challenge." But even some straightforward, plain-vanilla kinds of mergers and acquisitions could really see some sort of resistance, because they are going to be imposing some challenges for the status quo, some changes. If you are a chairperson today, and because of the merger you will be losing your chairmanship to be a vice president, or to leave, or to go to another institution, you are not going always to welcome that.*

But basically, there's an art. Again, the financial sector is very good at that, basically in preparing the road, paving the road through good communication, explaining your objectives—not just "This is because of that, and we are going to be doing it and that's it." They spent good time explaining why this was going to be happening. It is not just an art of applying democratic means of communication, but of getting the people engaged. Because—and this is every important—you do the merger and acquisition as one transaction, but people are going to be living together forever. So we need really this kind of introduction to minimize problems. There is never going to be a case of eliminating problems, but basically minimizing the problem.

IYER: Could you reflect on what the major successes of the financial-sector reform have been?

MOHIELDIN: *You need to attend the seminar. We will be—*

IYER: Yes, I'll definitely attend it.

MOHIELDIN: *You'll find many things.*

And well, the biggest test. Say you have a good goalkeeper—you have been training, but have never been tested. But you get the guy to play one of those big football teams and he manages to protect, as a goalkeeper, the objectives of his team. Well, this was basically the ultimate test. You check what happened before the financial crisis. And the biggest test to what happened was the financial crisis itself. So I think this was basically the ultimate test for the financial system of Egypt—as far as stability is concerned.

But now, as a person who is concerned about financial development, the challenges are basically in providing access to the financial sector, inclusive finance. Which is basically going to be my talk.

IYER: Yes.

MOHIELDIN: *All right.*

IYER: Yes, thank you so much.